

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking to Promote
Consistency in Methodology and Input
Assumptions in Commission Applications of
Short-Run and Long-run Avoided Costs,
Including Pricing for Qualifying Facilities.

Rulemaking 04-04-025
(Filed April 22, 2004)

ASSIGNED COMMISSIONER'S RULING AND SCOPING MEMO

1. Summary

This ruling and scoping memo describes the issues to be considered in this proceeding and the timetable for their resolution. As required by Rules 6(c)(2) and 6.3 of the Commission's Rules of Practice and Procedure (Rules), this ruling affirms the proceeding category and the need for evidentiary hearings, designates a principal hearing officer, and addresses the projected submission date of this proceeding, following a prehearing conference (PHC) in this proceeding on November 9, 2004.

This ruling also serves as notice of a joint PHC in this rulemaking and Rulemaking (R.) 04-04-003, to be held at 10:00 a.m. on January 24, 2005, at the Commission's Courtroom, 505 Van Ness Avenue, San Francisco, California.

2. Scope of the Proceeding

R.04-04-025 set forth a preliminary scoping memo for this proceeding, finding that this rulemaking should serve as the forum for developing a common methodology, consistent input assumptions and updating procedures for

avoided costs across various Commission proceedings, including Commission review of avoided costs for purposes of Qualifying Facility (QF)¹ pricing.

After considering the PHC statements and the discussion at the PHC, I elect to proceed with a phased approach for this proceeding, as generally recommended by the parties.

Phase 1: Use of the E3 Avoided Cost Methodology in the Energy Efficiency 2006-2008 Program Cycle

The first phase of this proceeding will consider the applicability of the now final E3 Report on avoided cost² for use in the energy efficiency investments for the 2006-2008 program cycle. Use of the E3 avoided cost methodology in this manner is recommended by E3, and is unopposed by parties in concept.

Although the E3 Report was developed for use in analyzing energy efficiency programs, this rulemaking, as originally issued, contemplated using E3's proposed methodology in all calculations and forecasts of avoided costs used in other Commission proceedings. The parties have had several opportunities to comment on the E3 draft report in this context subsequent to the issuance of R.04-04-025. Pre-workshop comments and replies on the Draft E3 Report were filed on June 4, 2004 and June 18, 2004, respectively. The Commission's Energy Division conducted a workshop on the Draft E3 report

¹ Qualifying facilities, or QFs, are qualifying non-utility cogeneration and small power production facilities under the Public Utility Regulatory Policies Act (PURPA) of 1978 that sell electric power to a host utility at the host utility's avoided cost rate. QFs are certified by FERC www.ferc.gov/industries/electric/gen-info/qual-fac.asp.

² *Methodology and Forecast of Long-Term Avoided Cost(s) for the Evaluation of California Energy Efficiency Programs*, E3 Research Report Submitted to the CPUC Energy Division, October 25, 2004. <http://www.ethree.com>.

from June 30 – July 2, 2004, and post-workshop comments on the Draft E3 report were filed on August 20, 2004, with post-workshop reply comments filed on September 3, 2004.

The final E3 Report, dated October 25, 2004, contains a response to parties' pre- and post-workshop comments in "Appendix E : Summary of Issues Raised by Parties." Appendix E in the final E3 Report is divided into six sections:

- Section 1: A brief statement of the qualities of resources that are best evaluated using the E3 avoided cost methodology.
- Section 2: A recommendation to adopt the E3 methodology for the evaluation of energy efficiency resources.
- Section 3: Applicability of the E3 avoided costs to other resources such as QFs, demand response programs, and distributed generation. These views are based on E3's participation in the July 2004 workshop, and review of the comments and reply comments received in this project. Parties have not had the benefit of a formal hearing or discovery process. As such, E3 presents these viewpoints as preliminary opinions only.
- Section 4: Discussion of issues that relate to the presentation of the avoided costs. The development of costs on an hourly basis by location is a significant departure from past practices and resulted in numerous comments requesting the re-expression of the avoided costs in the extant format.
- Section 5: Presentation of issues related to inputs to the E3 avoided cost methodology. E3 developed this methodology with the intention that it could be easily updated in the future. Accordingly, E3 believes that disagreements over particular inputs to the Report's avoided costs should be considered separately from proposed refinements to the methodology itself.
- Section 6: Brief discussion of the issues related to the avoided cost methodology.

These filings provide the Commission with an adequate record on which to consider the avoided cost forecast contained in the E3 Report for use on an

interim basis in the evaluation of energy efficiency programs for the 2006 program year. Since the 2006 programs are due to be filed in the first half of 2005, Phase 1 of this proceeding should proceed on an expedited schedule, with a draft decision on interim application of the E3 methodology anticipated by the end of February 2005.

Phase 2: Short-Run Avoided Cost (SRAC) QF Pricing

Another critical issue to be addressed in the near term in this proceeding is short-run avoided cost (SRAC) pricing for QFs. As described in the order instituting this rulemaking, the Commission, citing D.03-12-062 and D.04-01-050, found that there is a “pressing” need to revisit the SRAC pricing system, and that since “we have a two-year window until most QF contracts begin to expire,” a complete review of QF pricing was necessary. The Commission directed the parties to comment on which components, if any, of the methodology presented in the E3 Draft Report could be applicable to other avoided cost applications such as SRACs for QF pricing, but the two rounds of comments produced little consensus on this issue. Therefore, in light of the Commission’s findings in D.03-12-062, D.04-01-050, and the parties’ comments and PHC statements, and taking into consideration that QFs are subject to a number of federal and state legal requirements, an overview of which is provided in the OIR, I believe that a second phase of R.04-04-025 should address SRAC pricing. Specifically, the scope of Phase 2 of this proceeding should include all SRAC pricing issues, including, but not limited to: 1) whether or not the Commission’s current SRAC energy price formula, including existing time-of-delivery and line loss factors, should be replaced, and if so, what changes should be made, and, 2) updating current as-available and as-delivered capacity prices. In addition, as the Commission noted in the OIR, the scope of this phase will include an assessment

of whether the formula mandated by Section 390 of the Public Utilities Code allows us to assure just and reasonable rates for the power provided by QFs.

Certain parties also argue that the scope of the Phase 2 SRAC review should include development of a renewed fixed price option for QFs upon expiration of the current five-year pricing amendments adopted in D.01-06-015, and extended in subsequent decisions. However, the issue of whether the Commission intends to extend the fixed price option (or any other long-term policy option) is an issue that is pending in the QF policy phase of R.04-04-003. Specifically, on September 30, 2004, ALJ Wetzell issued a ruling in R.04-04-003 “initiating the Commission’s consideration of a long-term policy for expiring QF contracts.” The ruling stated that the determination regarding whether QF contracts should be extended, over what term, and the degree to which PURPA requires that the utilities purchase QF power would be addressed in R.04-04-003. Proposals regarding future QF policies and responses to those proposals were filed in R.04-04-003 on November 10, 2004 and November 26, 2004, respectively.

As noted in the September 30, 2004, ruling in R.04-04-003, the QF policy issues to be addressed in R.04-04-003 must be closely coordinated with the QF pricing issues under review in R.04-04-025. I agree. On January 24, 2004, a joint PHC in R.04-04-003 and R.04-04-025 will be held³ to address coordination and scheduling issues between the two proceedings. I encourage parties to communicate with each other prior to the PHC to identify areas where joint proposals might be appropriate or might assist in avoiding unnecessary duplication of effort.

³ ALJs Halligan (R.04-04-025) and Brown (R.04-04-003) will preside at this joint PHC.

Phase 3: Long-Run Avoided Cost Forecasts and Calculations

Consistent with the intent of the OIR, Phase 3 of this rulemaking will address the development of a common methodology, consistent input assumptions, and updating procedures needed to quantify all elements of long-run avoided cost across the various Commission proceedings, and adopt avoided cost calculations and forecasts that conform to those determinations. One of the issues to be considered in Phase 3 of this rulemaking will be whether to adopt the E3 avoided cost methodology to calculate long-run avoided cost for use in valuing Distributed Generation (DG), Demand Response (DR), and other resource options and programs. Resource options are valued according to their relative cost-effectiveness, specifically, comparing program benefits with program costs.

The E3 avoided cost methodology is not a cost-effectiveness methodology because it does not contain resource option profiles on EE, DG, or DR. The E3 avoided cost methodology just produces the baseline forecast of electricity and natural gas a utility would have to procure to meet a given load. Currently, the Commission has an established set of cost-effectiveness tests for use in valuing energy efficiency (EE) programs; however, the Commission has not adopted a similar set of cost-effectiveness methodologies for evaluating DG or DR. The EE cost-effectiveness tests are set forth in the Standard Practice Manual (SPM).⁴ The SPM tests require wholesale and retail rate forecasts. While the E3 avoided cost

⁴ *California Standard Practice Manual: Economic Analysis of Demand-Side Programs and Projects*, October 2001, as incorporated by reference in the Energy Efficiency Policy Manual. The Energy Efficiency Policy Manual was adopted as Attachment 1 to D.01-11-066. The *Standard Practice Manual* can be downloaded from the Commission's website, www.cpuc.ca.gov/static/industry/electric/energy+efficiency/rulemaking/resource5.doc.

methodology does produce wholesale power forecasts, it does not produce retail rate forecasts.⁵

In the DG Rulemaking, R.04-03-017, the Commission has stated its intent to coordinate on the issue of modeling with this avoided cost rulemaking,

R.04-04-025:

“Because of the timing of the Itron report and its obvious tie-in with the issues scheduled to be addressed in hearings, the ALJ recently rescheduled hearings on cost-benefit issues so the parties and the Commission may consider the findings and conclusions of the Itron report in hearings and a subsequent Commission order. We also intend to closely coordinate the modeling efforts in this proceeding with those in the proceeding in which we review energy avoided costs, R.04-04-025.” (D.04-12-045, p. 15, in R.04-03-017, emphasis added.)

In order for the Commission to evaluate the cost-effectiveness of DG programs, forecasts of avoided cost must be generated. It seems appropriate for us to address this issue in R.04-04-025. I will consider adding this Phase 3 DG issue to our schedule after a draft of the Itron report on cost-effectiveness analysis has been issued.

With regard to Phase 3 issues generally, the final E3 Report states that the E3 avoided cost methodology may require modification for application in QF pricing, demand response evaluation, distributed generation evaluation, and in the option value of electricity resources (e.g., comparing the value of certain renewable supply side resources with certain fossil resource alternatives).

⁵ Retail rate forecasts are a necessary input to the Participant Test in the SPM.

Alternatively, parties may propose other long-run avoided cost calculations and forecasting methodologies in Phase 3 of this rulemaking.

3. Procedural Schedule

Scheduling issues were discussed at the PHC and in PHC statements. Although I generally adopt the sequencing and intervals between filing dates proposed at the PHC, I have modified the schedule significantly to allow additional time for discovery and the preparation of testimony and rebuttal testimony in light of the pending discovery issues.⁶

In order to efficiently utilize hearing time, I will conduct a second PHC April 27, 2005 to schedule witnesses. I also set an April 22, 2005 date by which parties will be required to submit cross-examination estimates by witness, issue area, and disputed facts to allow us to set the schedule for evidentiary hearings. I encourage parties to attempt to reach agreement on how to allocate the limited time available for cross-examination between parties by that date.

⁶ A motion to compel compliance was filed on December 10, 2004, by the Cogenerators Association of California and the Energy Producers and Users Coalition (CAC/EPUC).

The procedural schedule in this proceeding is as follows:

Procedural Schedule		
Description	Phase	Date
Joint Prehearing Conference (PHC) with R.04-04-003	All Phases	January 24, 2005
Opening Testimony on Short-Run Avoided Cost (SRAC) Issues	Phase 2	February 25, 2005
Draft Decision on Use of E3 Avoided Cost Methodology in the Energy Efficiency 2006-2008 Program Cycle	Phase 1	February, 2005
Final Decision on Use of E3 Avoided Cost Methodology in the Energy Efficiency 2006-2008 Program Cycle	Phase 1	March, 2005
Concurrent Rebuttal Testimony on SRAC Issues	Phase 2	April 12, 2005
Scheduling PHC	Phase 2	April 27, 2005
Evidentiary Hearings for SRAC Issues	Phase 2	May 2 nd – May 13 th , 2005
Opening briefs for SRAC issues (including any request for oral argument before the Commission)	Phase 2	May 27, 2005

Reply briefs for SRAC issues	Phase 2	June 10, 2005 (submittal of Phase 2)
ALJ Proposed Decision in Phase 2	Phase 2	August 2005
Final Decision in Phase 2	Phase 2	September 2005

A schedule for Phase 3 will be established following release of the proposed decision in Phase 2.

This ruling affirms the Commission's intent to resolve all matters in this proceeding within 18 months of the date of this scoping memo, consistent with Pub. Util. Code § 1701.5.

4. Category of Proceeding

R.04-04-025 preliminarily determined that this is a ratesetting proceeding. The Commission invited objections to its initial categorization. No party has expressed any objection. This ruling confirms that the proceeding is ratesetting.

5. Need for Evidentiary Hearings

R.04-04-025 anticipated that hearings would be needed in this proceeding. The ALJ has correctly determined that evidentiary hearings are required for the Commission's resolution of SRAC issues. The Commission will determine at a later date whether to conduct hearings for Phase 3 issues. This ruling affirms the preliminary determination that hearings are required in this rulemaking.

6. Principal Hearing Officer

This ruling designates ALJ Julie Halligan as the principal hearing officer in this proceeding.

7. Service List

The service list for this proceeding is located at the Commission's Website (www.cpuc.ca.gov). Those who are not already parties, but who wish to participate in this proceeding as full parties must make their request by written motion to intervene, or orally on the record during the proceeding. Those not already participating, but who wish to do so as nonparties, may request that their names be added to the service list (in the "information only" or "state service" category) by sending an e-mail note to ALJ Halligan (jmh@cpuc.ca.gov).

The Commission will follow the electronic service protocols attached to R.04-04-025.

8. Procedure for Requesting Final Oral Argument

As stated in the schedule above, and pursuant to Rule 8(d), parties requesting final oral argument before the Commission should include that request in their concurrent opening brief, filed after hearing.

9. Rules Governing *Ex Parte* Communications

This proceeding is subject to Pub. Util. Code § 1701.3(c), which means that *ex parte* communications are prohibited unless certain statutory requirements are met (see also, Rule 7(c)). An *ex parte* communication is defined as "any oral or written communication between a decisionmaker and a person with an interest in a matter before the commission concerning substantive, but not procedural issues, that does not occur in a public hearing, workshop, or other public proceeding, or on the official record of the proceeding on the matter." (Pub. Util. Code § 1701.1(c)(4).) Commission rules further define the terms "decisionmaker" and "interested person" and only off-the-record communications between these two entities are "*ex parte* communications."

The law permits Commissioners to engage in *ex parte* communications if all interested parties are invited and with no less than three business days' notice. If a Commissioner agrees to meet with an individual party, the Commission must grant all other parties individual *ex parte* meetings of a substantially equal period of time. The law permits written *ex parte* communications provided that those who provide the letter to a decisionmaker must provide a copy the communication to each party on the same day. (Pub. Util. Code § 1701.3(c); Rule 7.) Parties must report *ex parte* communications as specified in Rule 7.1.

IT IS RULED that:

1. The scope of Phase 1 and Phase 2 of this proceeding is set forth as discussed above.
2. The schedule for Phase 2 of this proceeding, including the projected submission date, is set forth in this ruling. The assigned ALJ may specify the schedule for Phase 3 of this proceeding after issuance of a draft decision in Phase 2. The ALJ may make any revisions to this schedule necessary for the fair and efficient management of the proceeding.
3. This proceeding is categorized as ratesetting and evidentiary hearings are necessary, consistent with Rulemaking 04-04-025. This ruling on category may be appealed, as provided in Rule 6.4 of the Commission's Rules of Practice and Procedure (Rules).
4. ALJ Julie Halligan is the principal hearing officer in this proceeding.
5. This ratesetting proceeding is subject to Pub. Util. Code § 1701.3(c), meaning that *ex parte* communications are prohibited unless certain statutory

requirements are met. Such communications are also governed by Rule 7(c), and must be reported, as provided in Rule 7.1.

Notice of the January 24, 2005 PHC is being provided to parties to R.04-04-003 by ALJ ruling issued in that docket.

Dated January 4, 2005, at San Francisco, California.

/s/ Susan P. Kennedy

Susan P. Kennedy
Assigned Commissioner

CERTIFICATE OF SERVICE

I certify that I have this day served the attached Assigned Commissioner's Ruling and Scoping Memo on all parties of record in this proceeding or their attorneys of record by electronic mail to those who provided electronic mail addresses, and by U.S. mail to those who did not provide email addresses.

Dated January 4, 2005, at San Francisco, California.

/s/ Antonina V. Swansen

Antonina V. Swansen

N O T I C E

Parties should notify the Process Office, Public Utilities Commission, 505 Van Ness Avenue, Room 2000, San Francisco, CA 94102, of any change of address to ensure that they continue to receive documents. You must indicate the proceeding number on the service list on which your name appears.

The Commission's policy is to schedule hearings (meetings, workshops, etc.) in locations that are accessible to people with disabilities. To verify that a particular location is accessible, call: Calendar Clerk (415) 703-1203.

If specialized accommodations for the disabled are needed, e.g., sign language interpreters, those making the arrangements must call the Public Advisor at (415) 703-2074, TTY 1-866-836-7825 or (415) 703-5282 at least three working days in advance of the event.